Forex Outlook February 2013

Yohay Elam

Introduction

Welcome to February 2013 monthly report from Forex Crunch. 2013 began with a storm – volatility has risen in a wide variety of currencies: not only the yen is moving. The forces that moved currencies during January will be with us during February: currency wars, the disconnect between the improvement in European financial markets and the real economy, as well as the attempts to understand when the US will change its easing course. In addition, the Italian elections add a dose of uncertainty. These are the main themes awaiting us in the first part of the report.

Specific currency outlooks follow. Each currency outlook consists of two parts: a fundamental overview and a high time-frame technical analysis. In addition, the relative strength index tries to predict how major currencies will rank during February. A timetable of key events and some extra additional notes for Forex traders end the report.

As always, feedback is more than welcome. I'd love to hear your comments at yohay@forexcrunch.com.

Disclaimer

Copyright

Contents

Global Themes

US: Slow improvement and far less political uncertainty

The year began with ending the unfinished business left from 2012: the fiscal cliff. Politicians did kick some of the issues down the road, with the sequester awaiting us in February. However, markets are far more optimistic that solutions will be found – or are willing to buy temporary solutions as full ones.

Regarding the economy, the same trend of slow growth will likely continue. During January, the US reported a contraction in Q4 GDP, but as with Q3 growth, the devil is in the details.

Political situation

Late on New Years' Eve, US politicians made a deal regarding taxes: income taxes will go up only for households making $450K per year or more. A few more tax items were agreed upon, and one issue was left behind: **the payroll tax cut was not extended**.

This issue could have already hurt consumer confidence (as seen during January in the CB Consumer Confidence figure) and could be felt in retail sales numbers released in February. The full impact of this issue will be possible to asses only later on.

What was left behind?

Two issues: one is the debt ceiling, which was set to be reached towards the end of February. A motion to postpone this issue to the month of May was defused. The people in Washington probably wanted to avoid the debt ceiling debacle of 2011.

This approval, which joined the fiscal cliff resolution, had a significant impact: political matters came off the agenda very quickly. Rating agencies also liked the move and the threat of a credit rating downgrade seems far lower now.

It seems that the markets were **quick to buy the temporary solution as a permanent one, but perhaps they were right**: perhaps another last minute cliffhanger will not happen anymore, with the new Congress in place.

However, there is one issue still left for February: **the sequester**. The debt ceiling deal made in August 2011 included an automatic deal to reduce the long term debt: automatic spending cuts in both defense and non-defense expenditure. This was set for the end of 2012, assuming that the winner of the elections will get his way.

As we all know, the elections didn't change too much in the split political scene. When a deal was reached on taxes on New Years' Eve, the deal included delaying the sequester for two months. Politicians preferred solving the tax side before the spending side.

What will happen with spending? **It is safe to assume that a long term debt reduction plan will not be reached**. Democrats want more defense cuts and less welfare cuts, while Republicans want the opposite. They will probably agree on some small cuts in both fields, but the total cuts could be rather small. Yet again, kicking the can down the road.

If negotiations heat up and time passes by towards March 1st, the dollar could rise. Yet this time could be a bit different: with an early, watered down deal reached, and the issue staying away from the spotlight.

More slow growth

The headline GDP figure for Q4 was a shocker: the economy actually shrank by 0.1%, contrary to expectations. This figure will be revised during February. A revision to growth, even very modest growth, will be encouraging in the short term, while deeper contraction will be depressing.

In the longer term, it is important to look into the details: there are two main reasons for the contraction: a sharp drop in government spending, especially in defense, and a drop in inventories.

Both areas are volatile: defense spending jumped in Q3, and so did inventories. **When inventories are depleted, they need to be replenished**. This will likely happen in Q1 2013.

Other components of the GDP report are actually encouraging: consumer spending is up while the rate of saving is going up as well: the figures actually show an improvement in the situation of the US consumer. In addition, investment is up as well.

So, Q3 growth was strong: 3.1% and Q4 will probably be confirmed with a contraction. The general picture is closer to the annual growth rate for 2012: 2.2% - slow and frustrating yet continued growth in the world's No. 1 economy.

Fed Policy

At the end of January, the Fed left its policy unchanged, with open ended QE and low rate guidelines unchanged. The Fed continues expanding its balance sheet by $85 billion a month in buys of treasuries and MBS. The rates will only move when unemployment drops to 6.5% and as long as inflation expectations (for core inflation) remain under 2.5%. No dates are attached, and this remains dollar bearish.

In the meeting minutes of the QE4 decision, it was revealed that some members saw QE beginning to unwind in late 2013. Indeed, there are hawks on the committee: the new composition of voting members has a different hawk now: Esther George instead of Jeffrey Lacker. However, the hawks are almost extinct on the FOMC and **the Fed is controlled by the doves** – Ben Bernanke being the most prominent one.

During February, no Fed meeting is scheduled. If there is any potential for a change in policy, it will not come from various statements, but rather from job figures – this is the key to easing of the easing and some chance of monetary tightening.

Europe: Financial markets winning over real economy – for how long?

The surge of the euro during January was mostly driven by optimism about the debt crisis: there is a general notion that the worst is behind us. Bond yields of Spain and Italy fell and the need for a bailout including the "Men in Black" has eased as well.

Mario Draghi is seen as the hero: his London speech in July 26th, where he said he will do "everything to preserve the euro, and believe me, it will be enough" is the turning points. Draghi then followed through with the OMT, which proved to be a **big bazooka** – it wasn't used so far.

And the specific boost for the euro in January came from Draghi once again: he pat on his back and while saying "the jury is still out", he noted the change in the financial markets and expected to see "positive contagion" from the financial markets to real economy, in the second part of 2013.

Money that left the euro-zone during the worst days is now flowing in once again, pushing the euro higher; in a manner that is worrying many officials: a higher exchange rate makes exports less competitive.

The positive atmosphere can already be seen in forward expectations: German business confidence looking better and also purchasing managers' indices for January look better than earlier.

Real economy suffering, also from the exchange rate

However, the real economy is still struggling: the recession most likely continued in Q4: we will get full data during February. The economic contraction includes the biggest locomotive, Germany. Spain's unemployment rate reached 26% and Greece is not out of the woods.

As aforementioned, the higher exchange rate certainly weighs on prospects of growth. **The ECB is not expected to intervene in the currency wars**: this is not in its cook book. Politicians will likely complain, and make their complains loudest during the G-20 meetings in Moscow.

EUR/USD at the round number of 1.40 could not raise political noise but also trigger a significant pullback. The damage to the economies would loom heavily and could outweigh other forces that are battling in currency wars: the Fed with QE4 and Japan with its very determined deflation fighting policy, to name a few.

What Draghi can do is lower the interest rates: the recent fall of inflation to 2%, exactly the ECB's target will ease opposition from the Bundesbank. In addition, the ECB's own prospects point to a drop in inflation later in the year. A lower interest rate could help the struggling economies by making lending cheaper, as well as contribute to a lower interest rate.

After the ECB made a sharp turn from discussing a rate cut in December to a unanimous decision to keep rates unchanged in January, we cannot expect another U-turn in February. However, this cannot be ruled out during the spring.

Draghi dragged to the Italian elections

Another thing that could damage Draghi's success so far is his own conduct as the Governor of the Bank of Italy. During his reign, 2006-2011, an Italian bank named **Monte dei Paschi de Siena** got involved in a corruption and derivatives scandal. The case is somewhat complex and is still being investigated in Italy.

The case isn't discussed only in the economic and criminal sections, but also in the political ones. Italians go to the polls towards the end of the month. While the left bloc of Bersani is leading, current PM Mario Monti and former PM Silvio Berlusconi are also looking for voter support, as well as many other candidates.

Corruption is one of the issues in the elections and criticizing the BOI's role in failing to realize the situation in time has been common in all parts of the Italian political scene.

The case is likely to gain more traction during February, towards the elections, and **Draghi could find himself spending time defending his past actions rather than focusing on his current role as President of the ECB**. This could weigh on the euro.

Regarding the elections, the political risk is mainly if the new parliament is deeply split and no government could be formed. However, once a new government is formed, it is hard to believe that it will take any radical steps that step away from the current policy. The most favorable outcome for the markets is that the current PM, Mario Monti, will hold on to his post and continue the reforms. Yet also Bersani and Berlusconi are not likely to enforce a big change in policy, even if the campaign rhetoric could sound different.

The only force that has a totally different way of thinking is the 5 Star Movement led by former comedian Beppe Grillo. The party leads an anti-politician, anti-corruption stance, and Grillo expressed a thought about taking Italy out of the euro-zone.

The party gained traction a few months ago, when the situation was worse, and reached second place in opinion polls. Yet since then, the party fell in the polls. It could be a loud and effective opposition, especially regarding corruption, but it is very far from participating In power and changing the general course that is in line with the European Union.

Trying to Balance the Yen

The Japanese yen continued its downfall during January. The new Japanese government did not back down on elections promises. Officials continued talking down the yen directly and said that the yen is only "correcting" from excessive strength.

The pressure on the Bank of Japan continued and was somewhat fruitful: the BOJ announced more QE, set an inflation target of 2% and presented a program of open ended bond buying.

However, **the BOJ didn't go all the way**: the open ended program is only planned for 2014, and serves merely as a threat. In addition, the central bank's own targets for the medium term are for lower inflation levels than 2%.

So, the level of determination in the BOJ is still much lower than in the government. The current governor of the BOJ, Masaaki Shirakawa, is set to retire in March and Prime Minister Shinzo Abe already announced he would be looking for a candidate with similar views to his.

Abe must receive the approval of Japan's upper house of parliament for the candidate. The upper house is controlled by the opposition, at least for now. Elections will be held in July and the post needs to be filled in the meantime.

During February, the search and negotiations for a new government will be in full speed, and we can expect a new governor to be named during the month. The profile of this person will certainly impact the yen.

Currency wars become dangerous

In the meantime, Japan's peers are showing some discontent about its efforts to weaken the yen: comments about currencies from the two top figures in the euro-zone: German Chancellor Angela Merkel and French President Françios Hollande.

Towards the G-20 summit in mid-February, Japan might wish to lower the tone, and even express worries about the weakness of the yen. This would be politically wise: also the Chinese Yuan strengthens toward key international meetings, as a way to appease critics that blame it for currency manipulation.

An extremely weak yen could genuinely be dangerous for Japan: the nation depends on imports of fossil fuels for energy, and high prices could weigh on the country. In addition, Japanese bond yields remain well bid so far: the weaker yen and the rise in Tokyo's stock market hasn't deterred investors, mostly domestic, from Japanese bonds. These JGBs could lose their shine if the yen were to plunge too fast.

The next significant political milestone for USD/JPY is 95 – at the current pace of appreciation, this target could be easily reached during February. Also the round number of 130 for EUR/JPY could draw attention.

Ideally, Japan would like to see the yen weaken a bit more, but to see a more gradual process – one that would not anger its peers and would allow importers and exporters to adjust themselves.

During February, we could see some more fine balancing, especially in EUR/JPY that leaped over 1000 pips in January.

RORO is not dead, just resting

RORO is an abbreviation for Risk On / Risk Off. This has been the mode that characterized trading in the past few years after the crisis. In this mode, there was a high correlation between various assets: good news concerning the global economy (US data, euro crisis news, Chinese indicators, etc.) triggered a rise in stocks, and higher values for “risk assets”: oil, gold and risk currencies: practically every currency apart from the dollar, yen and the occasionally the Swiss franc.

Bad news, such worries about Greece, a Chinese slowdown or weak employment figures from the US, resulted in weakness in risk assets, together with a stronger dollar and strong yen.

See more in: Risk Factor – Explained.

During January, we saw a change: the better atmosphere weakened these correlations and let various currencies trade on their local indicators: the euro strengthened on debt crisis hopes, the pound fell on a new recession, the Canadian dollar dropped on a less-hawkish central bank, the Australian dollar struggled due to domestic weakness and the New Zealand dollar enjoyed optimism about the economy. Even the Swiss franc moved away from the EUR/CHF peg and found more life of its own, even if relatively limited.

Apart from the hopes regarding the European debt crisis, one of the drivers of this move was the release of the FOMC meeting minutes, which revealed that some members see an easing in monetary easing during 2013. If the US leads the world in growth, there is less risk and less “risk on / risk off”.

Are we back to the “old normal”? Not so fast.

The recovery in the US economy remains frustratingly slow and still fragile. We still await the acceleration in job creation which is what the Fed is waiting for. The January Fed decision showed that the committee is still in the hands of the doves.

In Europe, the crisis is still with us, even if it isn't in the headlines: without growth, it will be hard for the European economies to recover and lower their debt. The higher exchange rate is quite problematic for growth prospects. And regarding China, many doubts were cast about its economic kick start: doubts about GDP and a low official PMI cause worries.

Therefore, **it is too early to forget about the RORO correlation**. During February, we could see a mix of the "old normal" and RORO, but certainly not a return to the pre-financial crisis characteristics.

Currency Outlooks

This section consists of a fundamental country specific outlook and a high time frame technical analysis for each currency against the US dollar. The first part concerning the US dollar is only technical, referring to the US Dollar Index. For the euro and the yen, which had wild movements in January, a special coverage is available in the themes section, so the coverage is only technical below. All the charts are weekly charts.

- A description on the lines follows each section.
- For shorter term outlooks, please follow the weekly outlooks on Forex Crunch, linked in every section.
- If you prefer to view the charts on a web page, just click on the image.

US Dollar Index Technical Outlook

During January, the US dollar moved quite a bit, and eventually ended the month lower. Note that the downtrend resistance line seen on the chart has been modified from the previous monthly outlook. As the dollar made gains against some currencies and lost ground to others, the index remained in range.

Lines

89.62 is the post financial crisis high and is the final frontier on top. 88.70 is another peak, seen in May 2010, when the Greece received the first bailout.

86.87 is a minor line, serving twice as resistance in the early stages of the crisis. 85 is a round number that provided some support when the index was trading at a high level during 2010.

84.10 was the peak in 2012, from where the downtrend resistance line begins. 83.50 was the peak of an upwards move in the middle of 2010, before QE2 became reality. The line was challenged in August, but the index couldn't settle above this line.

81.80 served as support in 2010 and as resistance in early 2012 and now returns to working as resistance. The index failed to reach this level in the surge of

November 2012. 80.32 served as the top border of a tighter range. The bottom border of this range is 78.60, which was a cushion in April and also in January. This line worked perfectly well during September 2012 and will be tested if the index resumes its downfall.

In between, the 79.50 line serves as an important pivotal line within this range and it saw many battles over it.

77.50 is the next big support line. It worked as both support and resistance in 2009.

76 capped the long range trading of this index in 2011 and is strong support. 73.50 was the bottom border of that range.

The last line on the bottom is 72.70. For the major market movers, see the **Forex Weekly Outlook**.

EUR/USD Technical Outlook – Dizzy on High Ground?

Euro/dollar made over 400 pips in January, trading in a range of 600 pips.

The pair continued higher after the break above the steep downtrend resistance line which began in early 2011, from the high line of 1.4940.

A line that wasn't broken is the uptrend support line that began in mid-2012. The recent slide challenges this line. Note that the pair got away also from this uptrend and is now very moving vertically. Could we see some consolidation?

On the downside, there is steady uptrend support line dating from mid-2010, which is too low at the moment.

Looking at the bigger picture, euro/dollar is still in the wide downtrend channel that began just before the financial crisis. This is the higher black line.

Lines

The 2011 peak of 1.4940 is a significant line as well on the upside. 1.4580 capped the pair in 2011 and also worked as support in 2009.

1.4282 was the peak of the surge in November 2010. The round number of 1.40 is important mostly due to its political implications.

The swing low of 1.3838 seen in mid-2010 was also of important at the beginning of 2010 as a cap and as a separator back in 2008. There are no significant lines between this line and the next one. 1.34 is the top border of the sideways range and remains strong despite a temporary breach early in 2012, up to 1.3486.

1.33 was a stubborn peak at the end of 2012 and is key resistance. The peak of 1.3170 is now weaker after being broken, – it is the top of the trading range and served as a cushion when the pair traded higher. It was also a swing low in late 2011.

The round number of 1.30 is not only a psychological line but also used to be strong resistance. It was strong support and its break triggered a big fall. On the other side of the range sits 1.2805 – this line was tackled in the second half of 2012.

1.2587 is now a pivotal line that was seen in August and served as a stepping stone in September. It provided support during 2010. The first post crisis bottom at 1.2330 is now left behind after a struggle. It worked well as support. Despite being an old line, it is of importance.

For more on the euro, see the **EUR/USD Weekly Outlook**.

British Pound – Between a Rock and a Hard Place

The pound was one of the losers during January, and there are quite a few reasons to believe this will continue during February.

The British economy contracted 0.3% in Q4 according to the first release of GDP. The economy actually enjoyed only one quarter of growth, Q3, and this is clearly linked to the Olympics.

Another thing that hurt the pound was the option that the UK could leave the EU. This seems a remote option for the far future, but the ongoing debate about this in the UK already has implications on the British pound. Cameron's EU speech weighed on the currency as a "**Brixit**" poses risks to the economy – the UK still depends on trade with the continent. Worsening relations aren't good.

The EU has another impact on the pound: when things worsened in the euro-zone debt crisis, money fled from the continent to the UK. Now, the optimism from Draghi sends money to the EZ, and out of London.

We've already seen in the past that a weaker pound did little to help British exports and the economy. However, the impact on inflation, imported one, could be damaging.

BOE

The Bank of England is stuck between a rock and a hard place: launching more monetary easing in the form of a rate cut or QE could contribute some monetary stimulus, especially as yields are rising. However, as inflation refuses to drop, this could have unintended consequences.

The expected arrival of Mark Carney as governor of the BOE was greeted with cheers in the UK, as he is seen as a hawk. Yet recent comments from Carney show that he is acknowledging the weakness of the UK, and could oversee a dovish BOE.

Also the British government has a dilemma: the austerity measures don't really work and there is pressure to abandon the plan and move to Plan B: fiscal stimulus, in order to revive the economy. But on the other hand, this could cost the UK its perfect AAA credit rating. T

On this background of tough policy options, the pound could come under more pressure.

During February, statements from BOE officials will be important to note: the inflation report, meeting minutes and speeches will all matter more than the actual rate decision.

Not all is bad in the UK: jobless claims surprised with a drop, and manufacturing could be growing again, according to fresh purchasing managers' indices.

On the other hand, Britain's biggest sector, services, is contracting after a long time of growth. This is quite worrying. Also the housing sector isn't doing too good and retail sales disappointed with a drop.

GBP/USD Technical Outlook

GBP/USD made a false break above 1.63 and above downtrend resistance. This was the sign for the big downfall. The pair broke below uptrend support that accompanied the pair since mid-2012. The downfall is sharp.

Lines

1.7440 was a stepping stone on the way down during the peak of the crisis. 1.7042 is the post crisis peak reached during 2009 and never sought since. It is right above the round number of 1.70.

Below, 1.6750 was the peak of 2011 and also had a similar role during 2009. 1.6475 capped the pair several times in 2011 and is relevant is the pair succeeds in conquering 1.63.

1.63 was a peak in 2010 and later worked as a pivotal line. After many attempts to break higher and one big false break, the pair collasped. The round number of 1.60 also had a significant role in the past, and now plays the role of important support.

The trough of 1.5780 was of high importance in 2011 and also in 2009. It proved its strength as resistance in June 2012. Quite close by, 1.56 had an important role as a support line in 2012, and it now works as a pivotal line in the current range.

The double bottom of 1.5270 seen at the end of 2011 and the beginning of 2012 is the lowest points since 2010 and remains strong.

Below the round number of 1.50, we find 1.48, which provided an important cushion at the beginning of 2010. The bottom of 2010 at 1.4227 is significant on a big downfall. Last but least, we find the post crisis low of 1.3514.

For more on the pound, see the **GBP/USD Weekly Outlook**.

USD/JPY Technical Outlook – Time for Balance?

Dollar/yen enjoyed a fourth consecutive months of huge gains. The month of January saw another 500 pips. It's hard to draw downtrend or uptrend lines in such a steep surge.

Lines

High in the sky, 108 served as support before the financial crisis. 103.75 worked as support around the same era, 2008.

101.44 is the highest line here – it was a peak in early 2009 and serves as the beginning of a broken resistance line. The line is followed by the very round number of 100.

97.80 capped the pair in late 2009 and is the last important line of defense before the pair regains an extra digit. A very important line is 94.70 - which capped the pair for long months in early 2010. This is the next "political" target.

92.12 worked in both direction in 2009 and 2010 but is a weaker line after being broken. The ultimate support line in the shorter term is 90

Below, 89.10 was a peak in the summer of 2010, before the pair began descending. 88 was resistance back in 2010 and weakens now.

85.50 was the peak in 2011 after the coordinated intervention and is now support. 84.20 capped the pair back in March 2012. 82.87 was the line where the BOJ intervened in September 2010 and it played a role afterwards as well. It is currently a minor resistance line.

The round number of 80 was strongly guarded for some time and remains of psychological importance. It is now a line of struggle.

78 proved to be strong in the month of September despite the temporary dips. Minor support is at 76.60, which worked as support early in 2012.

76 was a previous all-time low and is now support in the range. The round number of 75, in uncharted territory might test the patience of the BOJ and the low of 75.57. A failure to guard this line has a potential of throwing the pair towards 70.

For more on the yen, see the **USD/JPY Weekly Outlook**.

Swiss Franc – More Breathing Room for now

During February, the franc got some more breathing space: the rise of the euro across the board underpinned EUR/CHF, which temporarily crossed the 1.25 line. The Swiss authorities could have used the opportunity to sell some excessive euros and buy some of their local currency – the franc eventually strengthened, with EUR/CHF falling to around 1.23, but it still keeps a safe distance from 1.20.

Speculation about a higher peg, of 1.25 has decreased. Also in the other direction, there is no chance of seeing the peg removed altogether. Prices in Switzerland are still falling: CPI dropped by 0.2% and this certainly provides the justification that the SNB needs in order to push the franc lower.

It is interesting to note that while Japan's currency policy comes under pressure from its trading peers, Switzerland is out of the limelight, and nobody considers labeling the country as a “currency manipulator”. Switzerland is not part of the G-20.

Also other figures support the policy: retail sales, the KOF Economic Barometer and the SVME PMI all remain pressured.

The franc could win against the euro during February, with EUR/CHF getting closer to the 1.20 line. As always, it is important to note that nothing lasts forever and that the levee could break, but this doesn’t seem likely right now.

Here are key economic releases in Switzerland for February:

- February 5th: Trade balance, a speech by SNB board member Fritz Zurbrugg.
- 7th: the SNB publishes its foreign currency reserves.
- 8th: Retail sales.
- 12th: Consumer Price Index (CPI) – more deflation?
- 13th: Producer Price Index (PPI).
- 21st: ZEW Economic Expectations
- 26th: Employment level

The next SNB meeting is held in March.

USD/CHF is falling towards 0.90, and remains technically interesting.

FOREX CRUNCH

USD/CHF Technical Outlook

January saw choppy trading for Dollar/Swiss, but eventually dropped to lower ground. Note the downtrend support that accompanies the pair since mid-2012.

Lines

1.09 capped the pair during 2010 and provided support beforehand. 1.0435 was support in 2010 and an area of struggle.

The round number of parity returns to the scene. It is backed by 1.0066. 0.9783 was a double top and provides strong resistance. It showed character in August 2012.

The round number of 0.95 worked as support and has psychological importance as well. After the breakdown, this line capped recovery attempts in September and in November 2012. It remains the top of the range.

0.9240 is the bottom of the current range, working quite well in October and November. It also provided some support back in March 2011. 0.9080, which was a trough recently, is also worth watching. The battle around this line is raging. Note that this line defends 0.90.

0.89, is another significant support line that proved its strength early in the year and also back in 2011.

0.8567 is worth mentioning on the downside. It served as support on the way down and then switched to resistance. Further below, 0.8330 was a strong line of support.

0.7820 is the final frontier before the big plunge to the all-time low at 0.7066.

Canadian Dollar – Housing vs. All the Rest

The Canadian dollar lost ground to the US dollar in January mostly due to a relatively dovish statement from the BOC. A rate hike is not that imminent. Did anybody think it was really coming that fast?

And, Canada's neighbor to the south has a much more dovish monetary policy – open ended QE, and lower rates until unemployment drops to 6.5%. Unemployment has just risen.

The Canadian economy is still doing very well:

- Unemployment dropped to 7.1% and the nation enjoyed a big gain in jobs in December. Good news is also expected for February. Canadian job reports can often be volatile, but the general trend is certainly positive.
- GDP for November rose by 0.3%, more than expected and showing a continued positive trend. With an improving situation in the United States, demand for Canadian goods remains strong.
- Oil prices are on the rise: WTI is not that far from the $100 line, and this supports the loonie. Optimism about global growth underpin the status of the C$ as a "commodity currency".

On the other hand, worries come from the housing sector: headlines like "how low can it go?", a drop in building permits, an expression of worries from the BOC and talk that the bubble is bursting all weigh on the loonie and could force a rate cut later in 2013.

No change in policy is expected in February. Mark Carney still has a few months as the head of the BOC, and he isn't expected to make any dramatic changes before he leaves.

All in all, the advantages that Canada has outweigh the disadvantages and a weaker loonie seems unjustified. So, after reaching 1.01, USD/CAD has potential to fall.

USD/CAD Technical Outlook

USD/CAD saw relatively sound movements during January and it became much more technically friendly. The pair continues trading within the wide narrowing channel. Note that during February, either uptrend support or downtrend resistance could be challenged.

Lines

1.1130 is an old line dating from 2009. It is still high. 1.0850 capped the pair in 2009 and 2010 and remains of high importance.

1.0677 also worked as strong resistance for many days, and was tackled again in Q3 2011. The round number of 1.05 is now a top in the range and can be challenged in the near future.

The round number of 1.03 was a battle line, and it seems that the pair overcame it. The 2009 low of 1.02, another round number, returns to the limelight.

The ultimate line of USD/CAD parity has a major role as the pair approaches this line from below. 0.98 returns to serve as an important cushion on the downside, where the pair bottomed out, despite the break lower.

0.9667 is a pivotal line on the way down, after working as support. The swing down to 0.9632 isn't significant at the moment. 0.9406 was the lowest post crisis level, and is the ultimate support line.

The 2007 of 0.9056 is way down.

For more on the Canadian dollar, see the **USD/CAD Weekly Outlook**.

Australian Dollar – Domestic Issues Weigh, China Ignored

The Australian dollar continued remaining in high ground, but it certainly lost its shine. The good figures from China, as seen in a healthy GDP report and an excellent manufacturing PMI reported by HSBC, have not helped the Australian dollar.

The Aussie also lost its shine as a "risk on" currency. Good news from Europe used to help the A$ in the past, as money was seeking risk and high yields. This correlation seems to have been broken.

The talk about "the end of the mining boom" hurt the Aussie in the past, and now they have less impact: commodity prices have been on the rise again, but this doesn't really boost the Aussie.

The biggest issues for Australia now come from within:

- **Retail sales** disappointed with a drop of 0.1% after remaining flat. Australian consumers are quite reluctant to buy.
- **Housing**: Quite a few developers are offering various "incentives" or "programs" to encourage buying of new homes. These are price cuts in disguise, and they point to some distress in the housing sector. Building approvals have disappointed as well.

- **Manufacturing**: PMIs from the Australian Industry Group (AIG) remain well below the 50 point line separating growth from contraction. The latest was quite discouraging: a drop to only 40.2 points.
- **Trade balance deficit**: Australia's trade deficit grew from 2.44 to 2.64 billion, instead of squeezing – this isn't positive for the currency of an export-oriented nation.
- **Less Swiss help**: The Swiss National Bank used to diversify its foreign exchange reserves from euros to other currencies, with the Aussie being one of their favorites. It is unclear if the SNB is selling A$ or just rebuying its own currency now that the situation has changed. But in any case, the Aussie isn't supported.

A notable fact that helps the Aussie is the lack of participation in currency wars: the RBA has no QE programs (US, UK, Japan and the ECB to some extent) nor is it intervening in the value (Japan, Switzerland). Without such activity, the Aussie is still supported.

The tool that the RBA does have is its interest rate: at the post crisis low of 3%, the RBA still has room to cut. No cut is expected for February, but the RBA tends to surprise its watchers, more than other central banks. Hints of a future cut could certainly come during the month.

All in all, the negative trends aren't likely to reverse in February, and the value of the currency might reflect the weakness more than earlier.

AUD/USD Technical Outlook

Yet again, 1.06 was challenged without success, and the Aussie seems to be losing momentum, despite the various breaks above downtrend resistance. This line is becoming less significant, while support at 1.0350 is now critical. Uptrend support is still far away.

Lines

The float-era high of 1.1080 is the ultimate line high in the sky. It wasn't a swing high but rather a significant hurdle. 1.0850 was a double top at the beginning of the year and is now resistance on strong upside moves.

The round number of 1.06 worked as support during two periods when the Aussie was trading higher. A third move towards this line didn't succeed, creating a triple top that is very important now. 1.05 capped the pair in November 2012 and also worked as support during 2011.

1.0350 was support during December and is notable now. It is the key to any downside moves. 1.0150 worked as support during September and October 2012 and is the bottom of the range. Breaking below this line will open the road to parity.

AUD/USD Parity is an important psychological line, although not so strong. 0.98 supported the pair at the end of 2010 and is minor support now.

0.96 provided an important cushion in September 2011 and also in June 2012. 0.94 is an important trough and also the cap of a long term range that lasted in 2009-2010. The round number of 0.90 will is of psychological importance.

For more on the Aussie, see the **AUD/USD Weekly Outlook**.

New Zealand Dollar – Strong Kiwi Could Backfire

The kiwi enjoyed quite a bit of strength during January, enjoying a healthy economy, good demand and a positive flip in its trade balance: from a deficit of around 500 million to a surplus of the same scale.

The RBNZ was certainly happy with the economic situation, but showed its discontent with the strength of the currency. The rising value of NZD makes exports less competitive and this could eventually be counterproductive for NZD.

However, in the near future, the kiwi could certainly challenge higher highs. The ongoing QE4 program in the US and the relative weakness of Australia could draw more funds into New Zealand.

February features the all-important employment data release. This is a quarterly event, contrary to monthly reports elsewhere. The scarcity makes it very important. Here are the main events to watch out for:

- February 4th: Labor Cost Index and ANZ commodity prices.
- 6th: Employment data. A gain of 0.4% in employment is expected, and the unemployment rate is expected to fall from 7.3% to 7.1%, boosting the kiwi.
- 12th: REINZ HPI
- 14th: Retail sales. Also here, this is a quarterly report, making it very important.
- 19th: PPI.
- 22nd: Credit Card Spending.

- 26th: Inflation expectations and trade balance.

One thing less to worry about is the scare regarding New Zealand's milk exports from Fonterra. At the time of writing, the milk has been declared safe. Milk exports certainly impact the kiwi.

NZD/USD Technical Outlook

NZD/USD enjoyed some strength during January but the 84.70 lines works as a perfect cap so far. The lower uptrend support line is very far. A newer, steeper support line accompanies the pair since mid-2012 and is becoming stronger. The pair will eventually have to choose between breaking above 84.70 or falling below uptrend support.

Lines

The round number of 0.90 is in uncharted territory. The float-era high of 0.8842 is the ultimate resistance line.

0.8470 was the peak in 2012 and remains key resistance. The pair temporarily breached this line, but didn't go too far. 0.8360 was a very impressive cap to the pair during September 2012 and is a key line on the upside.

0.8175 worked well as support during September 2012 and is only minor now. 0.81 is the bottom of the current range, after working as such several times in recent months and also at the beginning of the year.

0.7975, which was a veteran peak back in 2010 returns to play a significant role as the pair stabilizes above the line. A loss would open the door for bigger falls. The round number of 0.78 worked as support in early 2011 and also in mid-2012 and is the next line.

0.7650 capped the pair on recovery attempts and also worked as resistance in 2009. 0.7450 was a stubborn bottom in May 2012 and was also a swing low in the fall of 2011.

0.7350 is significant on the downside. The pair got close to this line during Q4. The round number of 0.71 was a swing low in 2011 and a break lower would be a bearish signal. Under the round number of 0.70, the next line of support is 0.6815, which worked as such in early 2010.

Relative Strength Index

January Revisited

1. EUR – EUR/USD rose 2.5%
2. NZD – NZD/USD rose 1.2%.
3. AUD – AUD/USD rose 0.3%.
4. CHF – USD/CHF dropped 0.5%
5. USD
6. CAD – USD/CAD rose 0.5%.
7. GBP – GBP/USD dropped 2.4%.
8. JPY – USD/JPY rose 5.5%

The predictions for January were quite good, apart from the strength of the euro. Note that all currencies apart from EUR and CAD ended the month exactly in the same ranking as predicted – EUR and CAD switched places.

1. CAD – The Canadian dollar could benefit from the fiscal cliff deal and "catch up" with other currencies. – Wrong, the Canadian dollar showed some weakness. This could be temporary though.
2. NZD – The kiwi could continue moving higher, enjoying internal stability. It hasn't reached a limit yet. – Correct. The kiwi made gains, riding on optimism, and finished second.
3. AUD – The Aussie remains under pressure, but could recover against the dollar and compete against its peer commodity currencies. Correct, the Aussie managed to make some gains and ended third, as predicted.
4. USD – The dollar could recover from QE4 as the US economy is improving. – Correct – the dollar was in the middle.
5. CHF – The franc could beat the euro in the peg race. – Correct, the Swiss franc ended in the middle.
6. EUR – With Germany slowing down and Greece never really getting out of the woods, the euro's rise could be somewhat reversed. – Wrong – the euro rode on Draghi's optimism.
7. GBP – After the failure to break higher, also the pound could reverse and slide in range. – Correct – the pound suffered from the triple dip recession and also from prospects that the UK could leave the EU.
8. JPY – While another 5% is unlikely, the yen could certainly end January as the weakest currency once again. – Correct, the yen was beaten once again and ended January as the weakest currency. Surprisingly, the drop was over 5% once again.

Predictions for January

1. NZD – The kiwi has potential to rise on the stronger economy, despite complaints about its strength.
2. CAD – The Canadian dollar could compensate for the surprising fall – it still has reasons to rise.
3. CHF – As EUR/CHF maintains a safe distance from 1.20, we could see the franc strengthen against the euro and against most currencies.

4. EUR – The euro's rise against so many of its peers seems unsustainable, especially given the implications for Europe. Results could be mixed this time.
5. USD – The dollar will likely see mixed results again, and lose a bit to the euro – not as much as in January.
6. AUD – The Aussie has quite a few reasons to fall, especially after refusing to do it in January.
7. JPY – After the free fall, the yen could end February weaker, but not against all currencies.
8. GBP – the fall of the pound hasn't fully materialized yet. After losing quite a lot of technical support, the pound could end the month on the lower side.

It's important to remember that these are merely speculations and not trade recommendations.

Key Events

Here are the key events that are set to impact currencies all over the world, larger than the scope of any individual country.

- February 1st: US Non-Farm Payrolls – first for 2013: +157K - within expectations.
- 5th: Australian rate decision.
- 6th: New Zealand quarterly employment data
- 7th: Australian employment data.
- 7th: UK Rate decision
- 7th: ECB Rate decision – more "positive contagion"?
- 8th: Canadian employment data
- 13th: UK Inflation report
- 14th: Japanese rate decision
- 14th: European GDP releases
- 14-16th: G-20 Summit in Moscow.
- 19th: European PMIs – they have a growing importance.
- 20th: UK Employment data

- 24-25th: Italian elections
- 27th: UK GDP (second release)
- 28th: US GDP (second release).

Sources for this report:

- FX Street Calendar (**available on Forex Crunch**).
- Forex Factory Calendar

Additional Notes for Forex Traders

Here are some additional notes for Forex trading during this month.

Volatility moving up

Volatility keeps on rising and rising. This provides opportunities, but also poses risks.

High leverage and wide stops can be disastrous to your trading account. When volatility is higher, reduce position sizes and minimize your risk. When volatility is lower, you can take a bit more risk, but don't gamble!

Apart from looking how to win in trading, it's important to limit your risk. Here are three basic methods for this.

Choosing a More Predictable Pair

Some pairs follow the rules of technical analysis in a better way, while others are quite unpredictable. This depends a lot on your trading system and on your style and these patterns change all the time. Nevertheless, here is a fresh list of the **5 Most Predictable Currency Pairs – Q1 2013**.

Resources

General Articles

- **5 Points on When to Go Pro** – Successful at forex trading and considering of doing it full time? There are a few steps on the way.

- **How to Choose a Forex Broker** – There are quite a few tools you can use before making this important decision.
- **Risk Factor Explained** – A deeper explanation about why the dollar falls on good figures and vice versa and under what conditions this will end.
- **Trading in Range or Catching Breakouts?** – What is your style? And what to look out for.

Recommended Sites:

- **TradingNrg** – For all you need to know about gold, oil and other commodities.
- **BO Crunch** – All you need to know about trading binary options.
- **ForexStreet.Net** – A great forex social site where you can interact with others.
- **Forex Live** – For the fastest updates on the web.

That's it! As I've mentioned at the beginning, I welcome feedback, comments, suggestions, complaints and anything you wish to tell me about this report. Please send any feedback to yohay@forexcrunch.com.

Happy forex trading!